

A great deal of literature determined the relation between financial development and economic growth; nevertheless many concerns still remain, for instance, the direction of causality and varying results with varying types of data and proxies for financial development.

In this study the finance-growth nexus in Pakistan has been assessed for the period of 1971-2011. The long-run relationship between finance and growth is investigated through the cointegration analysis. The ARDL approach is utilized to determine the link between financial development and economic growth along with some policy variables (share of investment, inflation and dummy as a representative of government reforms).

The results are found to be consistent with the studies as described in the literature, indicating that there exists a stable and positive relationship between financial development and economic growth in Pakistan for the period of 1971-2011. Bi-directional causality has been experienced among finance and growth. Furthermore, the share of investment and government reforms are found to be significant in playing a vital role for the financial growth nexus, whereas, the inflation rate has proved statistically insignificant. Finally, it is concluded that there is an ardent need to develop and stabilize the financial system in order to experience high growth rates.